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IN THE
Supreme Court of the United States

PHILIP MORRIS USA,

Petitioner,

v.

MAYOLA WILLIAMS,

Respondent.

On Writ Of Certiorari
To The Supreme Court Of Oregon

AMICUS CURIAE BRIEF OF A. MITCHELL POLINSKY, STEVEN SHAVELL, AND THE CATO INSTITUTE IN SUPPORT OF PETITIONER

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TABLE OF CONTENTS

Page

TABLE OF CONTENTS i

TABLE OF AUTHORITIES ii

INTEREST OF *AMICI CURIAE* 1

SUMMARY OF ARGUMENT 3

ARGUMENT 6

I. Increasing Punitive Damages In Light Of Corporate Wealth Does Not Serve The Objective Of Deterrence 6

A. There Is No Need To Enhance Punitive Damages To Reflect Corporate Wealth 7

B. Socially Undesirable Consequences Will Result If Punitive Damages Are Enhanced To Reflect Corporate Wealth 9

C. Punitive Damages Should Not Be Enhanced To Reflect Corporate Wealth 12

II. Increasing Punitive Damages In Light Of Corporate Wealth Does Not Serve The Objective Of Punishment 12

A. There Is No Need To Enhance Punitive Damages To Reflect Corporate Wealth 12

B. Socially Undesirable Consequences Will Result If Punitive Damages Are Enhanced To Reflect Corporate Wealth 16

C. Punitive Damages Should Not Be Enhanced To Reflect Corporate Wealth 17

CONCLUSION 17

TABLE OF AUTHORITES

Page

Cases

BMW of N. Am., Inc. v. *Gore*, 517 U.S. 559 (1996) 6

City of Newport v. *Fact Concerts, Inc.*, 453 U.S. 247 (1981) 6

State Farm Mutual Automobile Ins. Co. v. *Campbell*, 538 U.S. 408 (2003) 3

Zazu Designs v. *L'Oreal, S.A.*, 979 F.2d 499 (7th Cir. 1992) 13

Other Authorities

A. Mitchell Polinsky & Steven Shavell, *Punitive Damages: An Economic Analysis*, 111 Harv. L. Rev. 869 (1998) 3, 8, 14

Daniel Kessler & Mark McClellan, *Do Doctors Practice Defensive Medicine?*, 111 Q. J. Econ. 353 (1996) 10

David G. Owen, *The Problems In Assessing Punitive Damages Against Manufacturers of Defective Products*, 49 U. Chi. L. Rev. 1 (1982) 13

Don Dewees, David Duff, & Michael Trebilcock, *Exploring the Domain of Accident Law: Taking the Facts Seriously* (1996) 10

George P. Fletcher, *Rethinking Criminal Law* (1978) 12

Guido Calabresi, *The Costs of Accidents* (1970) 7

Herbert L. Packer, *The Limits of the Criminal Sanction* (1968) 12

Steven Shavell, *Economic Analysis of Accident Law* (1987) 7

Steven Shavell, *Foundations of Economic Analysis of Law* (2004) 11

W. Kip Viscusi, *Reforming Products Liability* (1991) 10

William M. Landes & Richard A. Posner, *The Economic Structure of Tort Law* (1987) 7

BRIEF *AMICUS CURIAE* OF A. MITCHELL POLINSKY, STEVEN SHAVELL, AND THE CATO INSTITUTE IN SUPPORT OF PETITIONER

INTEREST OF *AMICI CURIAE*[1]

A. Mitchell Polinsky is the Josephine Scott Crocker Professor of Law and Economics in the School of Law at Stanford University. He is also the Director of the John M. Olin Program in Law and Economics at Stanford Law School. Professor Polinsky holds a PhD in Economics from MIT and a Master of Studies in Law degree from Yale Law School, has taught at the Department of Economics at Harvard University and at Harvard Law School, and has been a professor of law and economics at Stanford since 1979. He is well known both nationally and internationally in the field of law and economics. His textbook, *An Introduction to Law and Economics*, has been used at over fifty law schools and economics departments in the United States. Professor Polinsky has written approximately seventy scholarly articles, mostly on the economic analysis of legal issues. He has served as President of the American Law and Economics Association, and has been both a Guggenheim Fellow and a Fellow of the Center for Advanced Study in the Behavioral Sciences at Stanford University.

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[1] The parties have filed blanket written consents with the Clerk to the filing of *amicus* briefs in this case. This brief was not authored in whole or in part by counsel for a party, and no person or entity, other than the *amici curiae*, their members, and their counsel made a monetary contribution to the preparation and submission of this brief.

Steven Shavell is the Samuel R. Rosenthal Professor of Law and Economics and the director of the John M. Olin Center for Law, Economics, and Business at Harvard Law School, as well as the co-director of the Law and Economics Program at the National Bureau of Economic Research. Professor Shavell has a PhD in economics from MIT, joined the faculty of the Department of Economics at Harvard University in 1974, and has been a professor of law and economics at Harvard Law School since 1982. He is an internationally known scholar in the economic analysis of legal issues and has worked extensively on tort law (he has published over twenty articles and a book in this subject area), as well as on litigation and deterrence theory. He is a past president of the American Law and Economics Association, is the co-editor of the *American Law and Economics Review*, is an elected fellow of the American Academy of Arts and Sciences and of the Econometric Society, and has been a Guggenheim Fellow. Professor Shavell has served as a consultant to government, including the Consumer Product Safety Commission, the Federal Trade Commission, the U.S. Department of Justice, and the U.S. Sentencing Commission.

The Cato Institute was established in 1977 as a nonpartisan public policy research foundation dedicated to advancing the principles of individual liberty, free markets, and limited government. Cato's Center for Constitutional Studies was established in 1989 to help restore the principles of limited constitutional government and to secure those rights, both enumerated and unenumerated, that are the foundation of individual liberty. Toward those ends the Institute and the Center undertake a wide variety of publications and programs. The instant case is of central interest to Cato and the Center because it concerns the due process implications of excessive punishment.

SUMMARY OF ARGUMENT

In the case at issue, the widow of a smoker brought suit against Philip Morris. The jury found Philip Morris liable for fraud and awarded $821,485 in compensatory damages (reduced to $521,485 under Oregon's statutory ceiling on damages for wrongful death) and $79.5 million in punitive damages. After the Oregon appellate courts upheld the full amount of punitive damages, this Court granted certiorari and remanded the case for reconsideration in light of *State Farm Mutual Automobile Insurance Co.* v. *Campbell*, 538 U.S. 408 (2003). On remand Oregon appellate courts upheld the full amount of punitive damages. Although the Oregon Supreme Court eschewed reliance on Philip Morris's wealth as a basis for upholding the punitive damages, the plaintiff has consistently relied on it in arguing that the punitive award is not excessive. Because she can be expected to do so again in this Court and because the issue of the proper role of corporate financial condition is an important and recurring one, *amici* believe that addressing that issue here may be of assistance to the Court. In examining that issue, we adopt a public policy, economic approach. Our conclusion, which has been articulated in part in A. Mitchell Polinsky & Steven Shavell, *Punitive Damages: An Economic Analysis*, 111 Harv. L. Rev. 869 (1998), is that the financial condition of a corporate defendant is irrelevant to either of the two goals of punitive damages.

Consider first the goal of *deterrence*, by which is meant inducing parties, through the threat of damages, possibly including punitive damages, to take adequate precautions and to otherwise behave in a socially responsible manner.

A common intuition holds that the wealth of a defendant is relevant to the magnitude of damages needed to deter. Deterring a millionaire from destroying his neighbor's flower garden out of spite will tend to require a higher level of punitive damages than deterring a person of average means—

because the millionaire will care less about having to pay any particular amount of damages than the average person.

This logic turns out to be valid only when the defendant's object is nonmonetary (for instance, the spiteful pleasure derived from destroying a flower garden). The logic does not apply when the defendant's motive is monetary. Then the defendant will be led to compare the monetary value of the benefit he would obtain from his contemplated improper behavior to the dollar damages he would have to pay, and the defendant will be deterred whenever the damages are greater—regardless of the defendant's wealth. Since the objective of corporations is monetary, the common intuition that the defendant's wealth should be taken into account in determining punitive damages does not apply to corporations.

Not only does the foregoing common intuition fail to apply to corporations, a closely related intuition—that a large corporation will alter its conduct only in response to large damage awards—is also invalid. Hence, we conclude that it is irrational to consider a corporation's wealth when determining the magnitude of punitive damages necessary to deter. In this case, the wealth of defendant Philip Morris should be irrelevant to punitive damages, with regard to the deterrence goal.

Moreover, if punitive damages greater than the level needed for deterrence are imposed, based on a mistaken belief that corporate wealth justifies enhanced damages, significant social disadvantages can result. As a general matter, inappropriately high punitive damage awards may lead corporations to take undue precautions, to charge excessive prices for products, and even to withdraw products from the marketplace. Additionally, imposing higher punitive damages on a corporation because it is wealthy acts as a tax on corporate success and is thus socially undesirable.

Second, consider the other goal of punitive damages, *punishment*, by which is meant penalizing blameworthy actors for their conduct. A common intuition holds that the wealth of a defendant is relevant to the magnitude of damages needed to punish. Punishing a millionaire will require imposing greater punitive damages than punishing a person of average means because the millionaire will care less about having to pay any particular amount of damages than the average person.

But this familiar intuition simply does not apply when the defendant is a corporation—for the basic reason that a corporation is not a person. Indeed, imposing punitive damages on a corporation often will not result in punishment of blameworthy individuals within it. A corporation may not punish its culpable employees or officers for a number of reasons, including that they may be hard to identify, may have retired, or may have died by the time punitive damages are imposed. Hence, the degree to which imposing punitive damages on corporations serves the punishment goal is considerably attenuated.

Still more attenuated is any connection between the wealth of a corporation and satisfaction of the punishment goal. Even if a corporation does penalize culpable individuals within it, there is no reason to believe that a wealthy corporation would penalize such individuals differently from a less wealthy corporation, and therefore no reason why the wealth of a corporation would matter to achievement of the punishment goal.

Unfortunately, and perversely, imposition of punitive damages on corporations tends to penalize individuals who bear little or no moral responsibility for corporations' wrongful acts. Specifically, the ones who tend to suffer the most from imposition of punitive damages are employees as a group, shareholders, and customers (because they may have to pay higher prices).

Hence, imposition of punitive damages on corporations, whether or not wealthy, does not tend to serve the punishment goal very well. The blameworthy may experience little or no punishment, whereas the relatively innocent may suffer the brunt of punitive damages.

The foregoing arguments lead to the conclusion that the factor of corporate wealth should play no role in determining the magnitude of punitive damages against Philip Morris.

ARGUMENT

As noted, we adopt a public policy, economic approach in our argument. In the first part below, we examine whether the wealth of a corporation should affect punitive damages in order to serve the deterrence objective of punitive damages. In the second part, we consider whether the wealth of a corporation should affect punitive damages in order to satisfy the punishment objective of punitive damages. These two objectives are the traditional goals of punitive damages that courts have endorsed.[2]

I. Increasing Punitive Damages In Light Of Corporate Wealth Does Not Serve The Objective Of Deterrence

A chief aim of tort law is to deter harmful behavior. This aim can generally be fostered by imposing damages, sometimes including punitive damages, on liable injurers, for that will tend to induce potential injurers to take reasonable

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[2] *See, e.g., BMW of N. Am., Inc.* v. *Gore*, 517 U.S. 559, 568 (1996) ("Punitive damages may properly be imposed to further a State's legitimate interests in punishing unlawful conduct and deterring its repetition."); *City of Newport* v. *Fact Concerts, Inc.*, 453 U.S. 247, 266-67 (1981) ("Punitive damages . . . are . . . intended . . . to punish the tortfeasor whose wrongful action was intentional or malicious, and to deter him and others from similar extreme conduct.").

precautions and to act in other ways to prevent harm. *See generally* Guido Calabresi, *The Costs of Accidents* (1970); William M. Landes & Richard A. Posner, *The Economic Structure of Tort Law* (1987); *and* Steven Shavell, *Economic Analysis of Accident Law* (1987).

A. There Is No Need To Enhance Punitive Damages To Reflect Corporate Wealth

Is the wealth of potential injurers relevant to the magnitude of damages needed to properly deter them? A common intuition is that a wealthy individual must face larger damages to be deterred than an individual who is not wealthy. Consider an individual who, because of a disagreement with a neighbor, contemplates destroying the neighbor's flower garden for his spiteful pleasure. To discourage this individual from committing his act, he must face a threat of damages that is sufficiently high to offset the spiteful enjoyment he would experience from destroying the flower garden. That level of damages will ordinarily be higher for a wealthy individual than for a poor one, for dollars usually have less significance to the wealthy than to the nonwealthy. Perhaps $5,000 would be required to deter a wealthy individual from destroying the flower garden, but only $500 would be required to deter a person of modest means from so doing.

The view that high damages are required to deter a wealthy party turns out on reflection to be incorrect when, unlike in the example just given, the motivation for an act is *monetary*. (The motivation for the bad act in the example was *nonmonetary*—it was spiteful pleasure.) When a party's motivation is monetary, the party will be induced by the threat of damages to compare the monetary gain he would obtain from his act against the dollar damages in the same way regardless of his level of wealth. Suppose that an individual could save $100 by not purchasing a safety device. Clearly, the individual would be induced to spend $100 on

the device if he would have to pay more than that amount in damages, such as $200, for failure to do so.[3] And importantly, the individual would buy the device under these circumstances whether he is poor or rich: regardless of his wealth, he would prefer to spend $100 on the device than to pay $200 in damages.[4]

Similarly, because the motivation of corporations is monetary, namely, to make profits, the common intuition that the rich need to face higher damages to be induced to behave appropriately does not carry over to corporations. A corporation, like the individual in the last paragraph, will want to spend $100 on a safety device in order to avoid a $200 liability payment. Doing so will be rational whether the corporation has annual profits in the thousands of dollars or in the billions of dollars.

An additional reason sometimes advanced for why large corporations need to face higher damages to be appropriately deterred is that such corporations are bureaucratic and thus will not respond to liability risks unless the damages that would be imposed are high. In other words, high damages are needed to attract the attention of senior management. But this view is mistaken as a general matter. Although large corporations typically have complicated organizational structures, with senior management at some remove from the level of operations, it does not follow that large corporations will tend to be insufficiently attentive to the reduction of risk. If the cost of a precaution is less than the damages incurred

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[3] There are some complexities to this argument that arise when liability is uncertain due to so-called risk aversion, but these are of second-order importance, as discussed in Polinsky & Shavell, 111 Harv. L. Rev. at 913.

[4] The distinctions just drawn between the contexts in which gains are monetary and nonmonetary are also discussed in Polinsky & Shavell, 111 Harv. L. Rev. at 913-14.

by not taking it, a large corporation will want someone employed by it to recognize that fact and take the precaution—because the corporation's goal is to maximize profits. A large grocery chain, for example, will want some employee at each of its stores to inspect that store's floor after it is mopped in order to ensure that it is not slippery. The corporation might delegate this responsibility to an employee low in the corporate hierarchy, such as an assistant store manager. That this task would not receive the attention of top management, as it might in the case of a firm consisting of only one or two grocery stores, does not mean that the task will be neglected or attended to inadequately. As long as a corporation expects to have to pay for the harm it causes, it will generally have proper incentives to delegate tasks so as to reduce harms.

In all, then, the high wealth of a corporation should not result in an enhancement of punitive damages for purposes of deterrence. It follows that the argument made by the plaintiff that the wealth of Philip Morris is relevant to the determination of punitive damages is unsound with regard to the goal of achieving proper deterrence.

B. Socially Undesirable Consequences Will Result If Punitive Damages Are Enhanced To Reflect Corporate Wealth

We have just explained that there is no reason for punitive damages to be elevated on account of the wealth of a corporation, and we now discuss why imposing such punitive damages exceeding the level needed to deter is socially undesirable.

First, excessive punitive damages may induce potential injurers to undertake socially wasteful precautions. For example, many scholars attribute the costly phenomenon of defensive medicine—the use of tests and diagnostic procedures that cost more than their expected health benefits—to excessive damages in medical malpractice

cases.[5] The problem of wasteful precautions can even apply to intentional acts, including fraud, because, for example, corporations could be led to spend excessively policing the behavior of their employees.

Second, excessive punitive damages raise product prices and thereby harm consumers. Product prices generally reflect the costs associated with production, which include liability and legal costs. If punitive damage awards are excessive, then product prices will be excessive, undesirably reducing consumption by consumers. Consumers will be discouraged by high prices from buying products not because of a real social cost associated with their production, but rather because of mistaken imposition of punitive damages by the legal system.

Third, excessive punitive damages may lead companies to cease selling certain products. For example, liability awards are thought to have been an important factor in the withdrawal of vaccines and general aviation aircraft from the market.[6] Some may believe, however, that driving cigarettes from the market would be a good thing, but the decision in the case at issue will have implications for punitive damages and the prices consumers pay across the spectrum of products and services.

Fourth, excessive punitive damages may spur excessive litigation. Litigation is a major cost for society and increases the burden on the courts. Indeed, it is estimated that in the

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[5] *See, e.g.*, Daniel Kessler & Mark McClellan, *Do Doctors Practice Defensive Medicine?*, 111 Q. J. Econ. 353 (1996).

[6] *See, e.g.*, Don Dewees, David Duff, & Michael Trebilcock, *Exploring the Domain of Accident Law: Taking the Facts Seriously* 241-42 (1996) (vaccines); W. Kip Viscusi, *Reforming Products Liability* 8 (1991) (private airplanes).

area of torts, litigation and associated expenses actually equal or exceed the amounts received by victims.[7]

Finally, tying punitive damages to corporate financial condition taxes corporate size and success. Indeed, the effective punitive damages tax would likely be levied at a rate that increases perversely with corporate size—because larger companies tend to have more extensive operations than smaller companies and thus commit more torts. Suppose that a typical punitive damage award were to equal some percentage, such as 1%, of net worth. And suppose also that corporations commit one punishable tort for every $100 million of net worth. That would mean that a company with a net worth of $100 million would pay punitive damages of $1 million, equal to 1% of its net worth, whereas a company with a net worth of $1 billion, would pay punitive damages of $100 million, equal to 10% of its net worth, because it would be involved in 10 punishable torts. Such an outcome is not only anomalous and irrational; it also predictably would deter business growth and mergers and create incentives to employ subsidiaries when a company might not otherwise do so.

In sum, if corporate wealth is employed as a factor that enhances punitive damages, punitive damages will tend to be excessive and result in substantial negative consequences for our social well-being. It would be a mistake to view the imposition of excessive punitive damages as a matter only of unfairness or legal impropriety.

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[7] *See, e.g.*, Steven Shavell, *Foundations of Economic Analysis of Law* 281 (2004).

C. Punitive Damages Should Not Be Enhanced To Reflect Corporate Wealth

It follows from the discussion above that punitive damages should not be raised to reflect corporate wealth. On one hand, we have explained that there is no affirmative reason to elevate punitive damages to accomplish deterrence of misconduct by wealthy corporations. On the other hand, we have stated why imposing excessive punitive damages leads to socially undesirable consequences. Hence, it is irrational for society to raise the level of punitive damages to reflect corporate wealth, given the deterrence goal of punitive damages, and irrational to impose greater punitive damages on Philip Morris in this case on account of the wealth of Philip Morris.

II. Increasing Punitive Damages In Light Of Corporate Wealth Does Not Serve The Objective Of Punishment

A second and distinct aim of punitive damages is punishment, namely, penalizing blameworthy individuals to a degree that reflects their culpability.[8] Increasing punitive damages in light of corporate wealth does not serve this punishment objective.

A. There Is No Need To Enhance Punitive Damages To Reflect Corporate Wealth

A common intuition holds that punitive damages should be increased to reflect the wealth of injurers in order to achieve the punishment goal. The intuition is based on the notion that the greater the wealth of a person, the less any particular damage payment will matter to him. Hence, the magnitude of punitive damages needed to create a desired level of disutility for a wealthy person would be greater than

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[8] On the general aim of punishment, *see, e.g.*, George P. Fletcher, *Rethinking Criminal Law* § 6.3.2, at 417 (1978); *and* Herbert L. Packer, *The Limits of the Criminal Sanction* 37 (1968).

the magnitude of punitive damages needed to create that same level of disutility for a poor person. It might be, for instance, that $100,000 of punitive damages would be needed to create a desired level of disutility for a millionaire, whereas only $1,000 would be needed to create the same disutility for a person with modest assets.

This common and largely correct intuition does not carry over to corporations for a simple but fundamental reason: A corporation is not a person, and thus imposing punitive damages on a corporation does not in any direct sense punish a blameworthy person.[9] Before considering the factor of corporate wealth, let us explain how, if at all, imposing punitive damages on corporations serves the punishment objective.

When the defendant is a corporation, the imposition of punitive damages often does not promote the punishment objective. This is because imposition of punitive damages frequently fails to result in the punishment of culpable

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[9] *See also Zazu Designs* v. *L'Oreal, S.A.*, 979 F.2d 499, 508 (7th Cir. 1992) (Easterbrook, J.) ("For natural persons the marginal utility of money decreases as wealth increases, so that higher fines may be needed to deter those possessing great wealth. . . . Corporations, however, are not wealthy in the sense that persons are. Corporations are abstractions; investors own the net worth of the business. These investors pay any punitive awards (the value of their shares decreases), and they may be of average wealth. Pension trusts and mutual funds, aggregating the investments of millions of average persons, own the bulk of many large corporations. Seeing the corporation as wealthy is an illusion, which like other mirages frequently leads people astray."); David G. Owen, *The Problems In Assessing Punitive Damages Against Manufacturers of Defective Products*, 49 U. Chi. L. Rev. 1, 16 (1982) ("[w]e must remember that the concepts of moral responsibility, punishment, and deterrence can mean vastly different things when judging the 'conduct' of an institution rather than of a human being").

individuals within the corporation.[10] It is true that corporations have an interest in discouraging conduct of their employees and officers that could result in damages, including punitive damages, and that corporations can seek to deter bad conduct through the use of internal sanctions, such as demotion and dismissal. However, several considerations suggest that the imposition of punitive damages on corporations will lead to less punishment of blameworthy individuals than might be supposed.

First, culpable employees and officers may not be punished by corporations because the corporations may have difficulty identifying them. Such individuals may be able to obfuscate their role in decisionmaking, which is often joint, or be able to conceal their behavior.

Second, even if culpable individuals within a corporation can be identified and punished, imposing punitive damages often will have little or no additional effect on their punishment. That is, the internal sanction imposed on such individuals may not be much (if at all) greater as a result of the corporation's bearing both punitive and compensatory damages than if the corporation had borne compensatory damages alone. When a corporation incurs high compensatory damages because of the blameworthy conduct of an identifiable employee or officer, it may want to levy whatever sanctions on him that it can; imposing punitive damages on the corporation then would not result in additional punishment of the individual.

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[10] We are here making the implicit assumption that if no culpable individuals are punished, the punishment objective cannot possibly be served. Under another conceivable view, however, the corporation would be treated as if it were a person, so that imposing punitive damages on the corporation would serve the punishment objective. We find such a view unappealing because a corporation is an artificial entity. *See* Polinsky & Shavell, 111 Harv. L. Rev. at 949-50.

Third, culpable individuals may simply be beyond the reach of punishment by a corporation because they have retired from the corporation or have died. This factor is particularly relevant in the present case, because the fraud for which Philip Morris was found liable occurred mainly decades ago.

Altogether, these factors make the satisfaction of the punishment objective uncertain and attenuated when punitive damages are imposed on corporations (as opposed to certain and undiluted when punitive damages are imposed directly on blameworthy individuals). The view that the imposition of punitive damages on a corporation automatically accomplishes punishment stems from anthropomorphizing the corporation and gives a false impression of reality.

Now let us consider whether raising punitive damages to reflect corporate wealth could serve the punishment objective. It is hard to see how. The level of punitive damages needed to induce a corporation to punish its culpable employees or officers ordinarily would not depend on its wealth. A $1 billion corporation and a $10 million corporation would both be expected to impose the same sanction on an employee for misconduct that resulted in a punitive damages award of a given amount. If the internal sanctions that corporations impose on culpable individuals within them do not depend on the corporations' wealth, as we would expect would normally be the case, the punishment objective will not be advanced by making punitive damages depend on corporate wealth.

To summarize, we have explained why the imposition of punitive damages on corporations is unlikely to foster the punishment objective, and that to whatever degree it does serve that objective, there is no punishment-related reason to raise the magnitude of punitive damages to reflect corporate wealth.

B. Socially Undesirable Consequences Will Result If Punitive Damages Are Enhanced To Reflect Corporate Wealth

Imposition of punitive damages on a corporation tends to penalize many individuals who are not blameworthy, a socially undesirable consequence given the goal of proper punishment.

One innocent group that may suffer when punitive damages are imposed on a corporation is the corporations' customers. The reason is that imposition of punitive damages may result in increased product prices, as we observed above, and thus reduce consumer welfare. Another group that may suffer is nonculpable employees and officers (culpable individuals are usually few in number), for punitive damages may put financial pressure on a corporation and detrimentally affect salaries and prospects for advancement. A third group that may suffer is shareholders, since corporate profits fall when punitive damages are imposed. Shareholders are normally dispersed and do not have a direct role in managing corporate affairs, so that their degree of moral responsibility for bad corporate behavior is low. (Indeed, shareholder responsibility is especially low when the wrongful conduct occurred decades ago, before most current shareholders made their purchases.) Significantly, these three groups—consumers, nonculpable employees and officers, and shareholders—are likely to bear the greatest part of the impact of punitive damages. In the case at hand, we suspect that virtually all of the $79.5 million of punitive damages will be borne by parties other than truly culpable parties, meaning that the imposition of punitive damages will in fact not serve the punishment objective.

It follows that to the degree that corporate wealth enhances punitive damages, the extent of inappropriate punishment of nonculpable parties will be increased, which is socially undesirable.

C. Punitive Damages Should Not Be Enhanced To Reflect Corporate Wealth

The logic of the two preceding sections implies that punitive damages should not be raised to reflect corporate wealth given the goal of proper punishment. We have explained that, as a general matter, the imposition of punitive damages on corporations is unlikely to foster the punishment objective because the truly culpable often are not punished, whereas those who are not culpable are likely to bear most of the impact of punitive damages. Against this background, raising punitive damages when corporations are wealthy serves no rational purpose and increases the amount of improper punishment.

CONCLUSION

The Court should reject any contention that the punitive damages can be justified on the basis of Philip Morris's financial condition.

Respectfully submitted.

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